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To All State and Local Government Employers:

Under a Memorandum of Agreement between the Commonwealth of Kentucky and the Internal Revenue Service, effective on January 1, 2017, both the taxable FICA wages and taxable Medicare wages will be calculated on the employees' gross wages rather than allowing a deduction of the employee's pension contribution. This settlement affects all State and Local Governmental employers within the Commonwealth of Kentucky.

This means that beginning next year, each governmental employer and their respective employees will each have to pay the increased amount of FICA and/or Medicare taxes. But, the additional contributions in the FICA taxes will result in increased Social Security benefits upon retirement. For CY 2016, the current FICA tax rate is 6.2% and the current Medicare tax rate is 1.45%

Thus, effective January 1, 2017 all Kentucky State and Local Governmental employers must calculate the FICA taxes and/or Medicare taxes on their employee's gross salary rather than reducing the gross salary by the employee's pension contribution.

The deduction was originally allowed based upon the term "*picked up by the employer pursuant to a salary reduction agreement*". The federal courts have redefined this sentence to mean that the employer themselves must pay the amount of the pension contribution for the employee rather than deducting it from gross salary when they forward the withholdings to the pension system for it to be recognized as picked up.

It should be noted that the income tax withholding calculation for the State and Local Governmental employee will not change. Their pension contribution deduction will continue to be allowed for the calculation of their federal and state income taxes.

Please contact J. W. Bryan, State Social Security Administrator at jw.bryan@ky.gov or at (502) 564-6879 if you have any questions.

